United States Senate

April 16, 2024

The Honorable Janet Yellen
Secretary
United States Department of the Treasury
1500 Pennsylvania Ave NW
Washington, DC 20220

Dear Secretary Yellen,

On April 9th, Deputy Secretary Adewale O. "Wally" Adeyemo testified before the Senate Committee on Banking, Housing, and Urban Affairs (Banking) on the threat cryptocurrency poses to our national security and the need for Congress to grant the U.S. Department of the Treasury (Treasury) additional anti-money laundering (AML) authorities to combat that threat. The Deputy Secretary's testimony highlighted a letter Treasury sent to Congress in November 2023 listing those necessary tools in the wake of Hamas's attack on Israel on October 7th.[1] Those authorities must be adopted into any legislation Congress advances to create a new regulatory framework around the $157 billion stablecoin market.[2] Folding stablecoins deeper into the banking system will supercharge trading in the crypto market, exploding the opportunities for terrorists and other bad actors to exploit those financing channels to both evade sanctions and receive a limitless stream of untraceable income.

A key provision from Treasury's November 2023 letter would apply anti-money laundering and combating the financing of terrorism (AML/CFT) requirements to the entire digital asset ecosystem, including payment intermediaries such as miners and validators. As the letter notes, "Parts of the digital asset ecosystem, including some decentralized finance (DeFi) service providers, noncustodial wallet providers, miners, and validators are not currently subject to [*Bank Secrecy Act* (BSA)] requirements. Hamas's use of both centralized exchanges and peer-to-peer transactions between unhosted wallets is well-documented. Validator node operators themselves have also posed national security concerns. Legislation making clear that these entities are considered a type of financial institution under the BSA

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[1] U.S. Department of the Treasury, "Potential Options to Strengthen Counter-Terrorist Financing Authorities," November 28, 2023, https://www.coincenter.org/app/uploads/2023/12/11.28.2023-Counter-TF-Legislative-Proposals.pdf.

[2] Cointelegraph, "Maxine Waters: Lawmakers 'very close' to a stablecoin deal: Report," Brayden Lindrea, February 8, 2024, https://cointelegraph.com/news/maxine-waters-legislators-very-close-deal-stablecoins; CoinMarketCap, "Top Stablecoin Tokens by Market Capitalization," April 12, 2024, https://coinmarketcap.com/view/stablecoin/.

would help drive compliance and enable stronger enforcement."[3] Miners and validators anonymously verify transactions on the blockchain. In exchange, they receive a fee or reward in crypto. During the hearing, I asked Deputy Secretary Adeyemo: "Is it possible that when I send [crypto] that Iran could be our validator and would be collecting a fee? All of that without either one of us knowing it?" He replied, "A transaction like that is certainly possible."[4]

Not only is it possible–it's happening right now. Iran made over $186 million dollars between 2015 and 2021 by validating crypto transactions.[5] One estimate indicates that Iranian Bitcoin mining could have produced as much as $1 billion in revenue in 2021.[6]

Financial regulators have recognized the reliance of bad actors and rogue nations on crypto financing, determining that crypto assets issued over public blockchains are highly unlikely to be consistent with safety and soundness principles.[7] The Federal Reserve denied a state-chartered crypto bank, Custodia Bank, membership in the Federal Reserve System in part on the grounds that crypto transactions could enrich bad actors. In its denial order, the Fed wrote: "The pseudonymity of crypto-asset transactions may also lead to financial institutions unknowingly but directly engaging in what may result in illicit financial activity. Crypto-asset transactions on some blockchains, including Ethereum, rely on distributed networks of anonymous persons for validation who receive transaction processing fees."[8] These fees "go to unknown validators, which may include illicit actors or sanctioned entities. To the extent a financial institution pays such transaction processing fees, it is risking making payments that support illicit finance or terrorist activity or to a prohibited jurisdiction or entity."[9] The Fed additionally cited Custodia's claim that it "is not aware of any way for it (or another submitter of transactions on the Ethereum blockchain) to prevent payment of a [transaction processing fee] in [e]ther to a sanctioned person acting as a validator pursuant to the Ethereum protocol."[10]

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[3] U.S. Department of the Treasury, "Potential Options to Strengthen Counter-Terrorist Financing Authorities," November 28, 2023, https://www.coincenter.org/app/uploads/2023/12/11.28.2023-Counter-TF-Legislative-Proposals.pdf.
[4] Senator Elizabeth Warren, "At Hearing, Warren Calls for Closing Gaps in Crypto Anti-Money Laundering Rules As Treasury Requested," press release, April 9, 2024, https://www.warren.senate.gov/newsroom/press-releases/at-hearing-warren-calls-for-closing-gaps-in-crypto-anti-money-laundering-rules-as-treasury-requested.
[5] Written testimony of Jonathan Levin to the U.S. Senate Committee on Banking, Housing, and Urban Affairs, March 17, 2022, https://www.banking.senate.gov/imo/media/doc/Levin%20Testimony%203-17-22.pdf.
[6] Elliptic, "How Iran Uses Bitcoin Mining to Evade Sanctions and "Export" Millions of Barrels of Oil," Dr. Tom Robinson, May 21, 2021, https://www.elliptic.co/blog/how-iran-uses-bitcoin-mining-to-evade-sanctions.
[7] President's Working Group on Financial Markets (PWG), Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Report on Stablecoins," November 2021, https://home.treasury.gov/system/files/136/StableCoinReport_Nov1_508.pdf; Reuters, "US congressional committee advances stablecoin bill," Hannah Lang, July 27, 2023, https://www.reuters.com/technology/us-congressional-committee-fails-reach-deal-stablecoin-bill-chair-says-2023-07-27/.
[8] Federal Reserve System, "Order Denying Application for Membership," January 27, 2023, p.33, https://www.federalreserve.gov/newsevents/pressreleases/files/orders20230324a1.pdf.
[9] *Id.*, p. 34.
[10] *Id.*, p. 40.

Treasury's efforts to counter terrorism and other illicit finance must evolve with the threat. As the Deputy Secretary noted in an exchange with Ranking Member Tim Scott, "while we can stop that money from financial institutions moving to Iran, I do not have the authority to stop cryptocurrencies from moving into Iran."[11] Excluding miners, validators, and other intermediary nodes in the DeFi system from the stablecoin legislation's AML/CFT requirements would allow bad actors to profit from the increase in crypto trading that stablecoin legislation would provide.

Those bad actors are hurting real people. Deputy Secretary Adeyemo relayed an alarming exchange he had earlier this week with the families of hostages still held by Hamas. When asked by those families how Hamas still has access to financing despite exhaustive sanctions and Israel's blockade, "I explained to them the actions we are taking in the traditional financing sector, but told them, frankly, that one of the places where we need additional tools is to be able to make sure that we don't allow Hamas to build up assets in the digital ecosystem using virtual currencies that are hard for us to track. Because that is money they will use to continue to come after not only Israel, but also to destabilize the region."[12] Since 2020, in the years leading up to the October 2023 attack, Iran has relied on crypto to send large sums of money to Hamas.[13] The Treasury Department is currently investigating $165 million in crypto transactions over the past three years that may be linked to Hamas.[14]

My colleagues on the Banking, Housing, and Urban Affairs Committee across the aisle are also disturbed by the scale of this problem, which extends well beyond transactions involving sanctioned entities. During the hearing, Senator Tillis acknowledged: "Cartels now–it's passé to launder the old way–cartels use digital and crypto platforms to launder at scale, and I mean in the billions."[15]

Any legislation that enhances the attractiveness of crypto to ordinary crypto traders will multiply money-making opportunities for sanctioned entities like Iran and the criminal underground. In Deputy Secretary Adeyemo's words: "Everything we have seen says that when markets grow, threat actors use them more, and we should expect that is what would happen here as well."[16] Stablecoin legislation, which will grow the crypto market and

[11] Senate Committee on Banking, Housing, and Urban Affairs, "An Update from the Treasury Department: Countering Illicit Finance, Terrorism, and Sanctions Evasion," April 9, 2024, "https://www.banking.senate.gov/hearings/an-update-from-the-treasury-department-countering-illicit-finance-terrorism-and-sanctions-evasion.

[12] Senate Committee on Banking, Housing, and Urban Affairs, "An Update from the Treasury Department: Countering Illicit Finance, Terrorism, and Sanctions Evasion," April 9, 2024, https://www.banking.senate.gov/hearings/an-update-from-the-treasury-department-countering-illicit-finance-terrorism-and-sanctions-evasion.

[13] Wall Street Journal, "Hamas Needed a New way to Get Money from Iran. It Turned to Crypto," Angus Berwick and Ian Talley, November 12, 2023, https://www.wsj.com/world/middle-east/hamas-needed-a-new-way-to-get-money-from-iran-it-turned-to-crypto-739619aa.

[14] *Id.*

[15] *Supra* note 13.

[16] Senator Elizabeth Warren, "At Hearing, Warren Calls for Closing Gaps in Crypto Anti-Money Laundering Rules As Treasury Requested," press release, April 9, 2024, https://www.warren.senate.gov/newsroom/press-releases/at-hearing-warren-calls-for-closing-gaps-in-crypto-anti-money-laundering-rules-as-treasury-requested.

opportunities for terrorist fundraising, must include the full suite of AML tools that Treasury requested in its November 2023 letter to Congress as necessary to effectively combat that threat.

Sincerely,

Elizabeth Warren
United States Senator